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HEADLINE: MARKET PRICING 101: The Science and the Art

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BODY:

QUICK LOOK

* Staying abreast of new developments will keep compensation professionals ready and able to meet the challenges placed on them as the company's market pay experts.

* Using market data effectively helps the business present its market pay position to employees logically and consistently.

* Selecting the right survey sources is predicated on a good understanding of the business and how it relates to the market.

Whether you are a seasoned veteran who market prices 200 jobs a year or you are newly charged with converting your company's 20-year-old point factor system to a market-based pay philosophy, the world of salary surveys - just like the stock market - is ever changing. Staying abreast of new developments will keep you ready and able to meet the challenges placed on you as your company's market pay expert.

The effort to balance current payroll against the market is critical because of the need to attract, retain and properly motivate the best people. In this Web-access world, one can assume that every employee has a good idea of how much his or her co-workers earn in terms of base salary. Using market data effectively helps the business present its market pay position to employees logically and consistently. While an employer's market position is important, the consistency with which market data is collected - and the consistency in creating supporting pay policies around that market - is what creates an atmosphere of employee commitment.

Step One: Acquire the Right Data

There are a variety of surveys from many different sources available every year. Selecting the right survey sources is predicated on a good understanding of the business and how it relates to the market. To start, there are a few questions that need to be answered:

* From which market do I hire employees?

* To what market am I losing employees?

* In which market would my company like to compete?

The answers to these questions will create a description of a company's market position and lead to the survey sources that provide data relevant to a specific market. You may find that different job groups have different markets. If so, then different survey sources are needed for different employee populations or, at the very least, a survey that has the

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data cut (i.e., the way a vendor separates data, such as by geographic location, number of employees or market segment) the company requires. (see "Market Comparators.") Market Comparators

After determining the market your company competes in (or the one it wants to compete in) based on its job groups, it's time to select the surveys. Survey vendors will willingly review the participant and job list available in their surveys. Clearly describe to the vendor the market comparisons that best represent the business, then determine how many of your company's positions are represented in the selected survey's job list. It is relatively easy to find surveys for jobs that are common to many industries (e.g., administrative assistant), and a good all-around survey will have most of these jobs available.

It will be more challenging to find survey sources when looking for executive jobs, unique industry jobs and/or sales jobs. There are resources, such as Survey Sources for U.S. and International Employee Pay and Benefits published by Personnel Systems Associates, that can help focus the search. While the cost may be more per useful market data point due to the specialized nature of the data, it may be worth the money because it's the only way to obtain the necessary data.

Surveys come in all price ranges and many formats beyond the traditional paper reports. PDFs, electronic and Web-based tools provide flexibility that was not practical just a few years ago. Choose the format that works best for your company. Depending on the number of pricings you expect to conduct annually, one system may be more cost effective than another. Many vendors (e.g., Radford, McLagan, etc.) maintain compensation Web sites that allow users to review the qualification of the survey, costs and methods for delivery before purchasing.

Light users (i.e., fewer than 50 jobs annually with minimal analytic requirements) will find that buying a printed or PDF report is sufficient, as data can be manipulated via in-house spreadsheets. "Power" users (i.e., more than 50 jobs annually with or without fairly extensive analytic requirements) will find electronic versions more easily manipulated and shared among stakeholders.

Power users should consider some form of Web-based market pricing tool that enhances the use of the electronic data and facilitates the process of creating composite pricings (multiple survey jobs and sources). These tools will cut the time commitment for market pricing and even survey submission in half. Plan how much administration is necessary for the market pricing effort, and then make sure you have the surveys and systems to meet the demand.

Club, Industry-Specific and Local Surveys

Surveys come in all shapes and sizes. Many companies participate in and subscribe to club, industry-specific or local surveys.

* Club Surveys. Provided via a professional organization. Participating in and receiving data from the club survey is a privilege of membership. Local and industry-specific surveys can be club surveys. These surveys are chosen when they closely represent a company's market position and the data cannot be found more economically elsewhere.

* Local Surveys. Often provide a number of general-industry entry-level positions. To find local survey data, check with local HR organizations to see if they can provide the name of a local survey provider.

* Industry-Specific Surveys. Usually provided via a professional organization specific to the business.

For a survey to be useful, the participant list, survey jobs and specific data cuts must be relevant to the company's established market position. Evaluate the quality of the data before committing to purchase. Review the provider's methodology. Many of the following facts will be described in that section:

- * Number of participants
- * Data collection period
- * Excluded data and reasons
- * Positions included
- * Type of data cuts available, industries, geographics, etc.
- * Information about the survey vendor.

If you choose to buy a club survey, you may have an opportunity to participate in creating the survey jobs and methodology for data collection and analysis. This is a good opportunity to ensure that the survey provides your com-

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pany with the positions and data you need most. Note of caution: The survey jobs should always be generic enough to ensure comfortable matching by selected businesses outside of your own.

Custom Surveys

Despite the array of surveys available, there are many underrepresented niche positions or industries. Custom surveys can help define these hard-to-reach markets, and can answer unique, qualitative questions (e.g., the frequency of the incentive payout). If you choose to conduct a custom survey, choose a partner with experience collecting and analyzing compensation data. Current laws and trends in governance strongly suggest that a "disinterested" third party conduct salary surveys. A good partner also will ensure that each survey question is designed to elicit the quantity and quality of answers most useful to you, the survey sponsor.

Step Two: Defensible Market Pricing

After developing the market position and selecting the surveys, it's time to begin the market-pricing task. Experts agree that jobs should be priced based on job content alone, so make certain that you have reliable documentation before pricing positions. Collect job codes, titles, families and descriptions for the jobs being market priced, along with:

- * Base pay data
- * Bonus pay data
- * Long-term incentive data
- * Demographic data (e.g., department, location, budget code, etc.)
- * Other incumbent data relating to company jobs.

Depending on how this data is stored, assistance from a member of the company HRIS staff may be needed to gather this additional information. Next, organize position data upfront. Think through how the company will want to compare the data (e.g., by business unit, budget code, department, job functions and families, etc.).

Position Matching

Select a family of jobs to price, then organize the jobs by their natural hierarchy. Select the job at the bottom or top of the hierarchy and match that job first. This will establish an anchor job.

Job matching is the process by which a company's jobs are matched to a survey's jobs. Many survey vendors offer job-matching conferences. These provide excellent opportunities to validate the matching exercise and ensure that you are using the same measuring stick as other compensation experts.

To get started, read your job documentation and note the facts about:

- * What the job does
- * How much experience is necessary to do the job
- * Who the job reports to
- * Whether the position has supervisory or management responsibilities
- * The extent to which the successful completion of the job's content affects the company's overall success.

This process is called leveling. It is important to understand the level of the company position and the level of the positions documented by the survey.

The importance of job matching cannot be overstated. It is critical to carefully choose matches and document the reasons for selecting each match; clients and business leaders will challenge the matches. If there are questions about the job responsibilities for an in-house job, call the supervisor and review the responsibilities. If there are questions regarding the vendor's survey job description, call the vendor for clarification. After selecting the job match and level, it's time to select the data cut.

Selecting a Data Cut

This goes back to the very first step. When you considered potential survey sources, you also considered how to best describe the market. Selected data cuts should follow your market (i.e., if you determined that the company is a

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pharmaceutical firm with revenues of \$1.5 billion and those options exist in the survey, the data cut is an accurate reflection of the company's market position).

Note of caution: It is important to be consistent throughout the process to create credibility. The surveys and data cut selections always should be consistent. If you cannot find adequate representation for your chosen market, then drop the qualification that makes the choice too narrow. In the case of the \$1.5 billion pharmaceutical company that employs 500 people, the qualification to cut likely is the number of employees. After making the decision to broaden the scope of your search, stick with that search for the remainder of the market pricings. Some matches may have to be dropped because they do not have reasonable market comparators. This is expected, and you will have a more defensible analysis when providing the business with an apples-to-apples study.

After determining that the survey job and the company job are a good, defensible match, the next step is to determine the quality of data. General parameters include:

- * Number of Companies in the Match. Data are less reliable with fewer companies. Usually, surveys will not report less than five company matches. Typically, five offer the best opportunity for a decent data range.

- * Number of Incumbents in the Match. Data is less reliable with fewer incumbents. Some jobs can be expected to be one company and one incumbent, but you should only accept these ratios when it makes sense based on your understanding of the job content.

- * This Year's Data vs. Last Year's Data. Note: This requires two years of data. An analysis can be conducted to see if the trend is reasonable, but the definition of "reasonable" is variable - it depends on the market. Consider the technology industry as an example. In the past two years this segment's salary data has slowed considerably and there are no expectations that the data will move much up or down. If there is a jump in the data, some investigation is necessary to determine where the data is coming from and whether there has been a change in quantity or quality of data providers.

If after close examination you do not feel that using a particular data point is good, throw it out. Remember: Using bad data erodes your professional credibility and the company's ability to rely on the market.

Data Adjustments

What if the match is pretty good, but not perfect? Vendors place the most important job responsibilities in the first sentence of the position description. Based on this parameter, try to achieve at least an 80-percent match. A plus or minus 20-percent adjustment (i.e., a job content adjustment) is acceptable, provided the survey data does not have a better match and you are reasonably content with the match. To defend your position, document your reason for creating an adjustment to the data point. Not only will the documentation help defend the market position, it will help re-create your work next year - long after you've forgotten why you chose this path in the first place.

Other adjustments can be made and should represent the position match and the company's market position. The following adjustments are common:

- * Aging the data
- * Geographic adjustments
- * Leading or lagging the market.

Data should be aged consistently. Vendors collect market data as of a specific effective date. That data can be aged to today or to some point in time that is relevant to your organization. Survey sources may have different effective dates, so the apples-to-apples rationale applies. Remember: Pick one date and stick with it.

The first question to consider is how much to age the data. One option is to age all data to the market's reported annual change rate, which is found in the pay practices section of the selected surveys and/or in one of the merit increase and salary structure annual surveys. Many companies will pick one aging percent (e.g., 4 percent) and use it across company jobs, surveys and various measures (i.e., base pay, bonus pay, long-term incentives). A case can be made for variability; for example, officer positions versus all others. Often these populations have different aging rates. A case can be made for a different aging percentage for base salary and variable pay. Again, if the market supports it and it can be used consistently, it could be a valuable tool for creating your defensible position in the market.

Geographic adjustments usually are made to data points when the position is hired locally, but the data is collected nationally. Take, for example, the position of administrative assistant. If you collect national data for the position but

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need to attract and retain in Manhattan, you will find that you need to make an adjustment to the original data to ensure a competitive rate. Geographic adjustments typically are applied to the market pricing once it is complete.

Finally, a company may choose to lead or lag the market in a particular sector or job group to reflect a business position. If a company has a group of jobs that are key to the business, it would be effective to lead the market. In this case, consider adjusting the market data position by some agreeable percentage to reflect the company's commitment to the position.

Survey Composites

The use of three or more survey sources is recommended. Remember: Despite a vendor's best efforts, levels of organization participation change annually. As such, there will be some variability in every survey source. Using several different sources creates less variability for pricings just by creating a larger data pool. The market pricing that results from the combination of several survey sources is called a composite. Composites can be created in several ways:

- * Simple average of the data points

- * Employee weighted (the weighted average based on all reported employee data points, when the survey vendor provides data this way)

- * Company weighted (the weighted average based on the number of companies providing aggregate data, when the survey vendor provides data this way).

Difficult-to-Match Jobs

Most companies have a number of jobs that are not easy to match. This typically requires a bit of creativity. Sometimes the position is a combination of jobs that can be matched independently; for example, the manager of housekeeping and the manager of engineering. If one incumbent holds both jobs, then a blended approach may be the best way to go. There are a couple of questions that can help guide this process:

- * What percent of time does the incumbent perform duties for Job A? Job B?

- * Are the skills, experience and/or education more or less for one of the jobs?

Based on your answers, you can apply a relative weight to the two jobs and combine them 50/50 or 80/20 or whatever the case may be.

Another technique is to match the job to a matched internal job, then apply an adjustment factor commensurate with the difference between the positions, not more than 20 percent up or down. If the adjustment is up, it is called a premium. If the adjustment is down, it is called a discount. This technique indicates that the two jobs are similar in content, but one is bigger or smaller than the matched internal job.

When making adjustments and allowances, document the work. As stated, this adds credibility to the pricing and it sets you up for successfully re-creating the work next year.

Benchmarking

Benchmarking is the practice of choosing a sample of the total number of jobs in the company for the market-pricing analysis. This usually is done when it is not necessary or economical to market price all positions in a company. A few tips for successful benchmarking include:

- * Try to price 30 percent to 50 percent of the jobs

- * Select jobs from each job family

- * Include jobs that are common to many companies and can be reliably found in the survey data, along with a few jobs that you think will be hard-to-find positions.

As a starting point, use a first-level job and the highest executive job in the study, along with selected positions in that range. This will help frame all positions and ensure they are appropriately anchored in the market. The jobs that you do not market price will need to be "slotted" into the organizational hierarchy after you are satisfied with the benchmarked market pricing results.

Successful Market Pricing

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Upon completion, check pricings against the current incumbent average, job by job. When the market and current incumbent pay levels are markedly different, experienced market analysts evaluate the company's documentation, then the incumbent's history and contributions to determine the reason for the mismatch. It may be that the job is undervalued or overvalued, or perhaps the job documentation is inaccurate. Every aspect of the job should be analyzed to ensure accurate matches. This is the cornerstone of the market-pricing process. Once the process is complete, you are ready to start using your data to analyze your company's position against the market.

RESOURCES PLUS

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WHEN MAKING ADJUSTMENTS AND ALLOWANCES, DOCUMENT THE WORK.

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